

## Message Text

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ACTION ARA-10

INFO OCT-01 ISO-00 SP-02 USIA-06 AID-05 EB-07 NSC-05

CIEP-01 TRSE-00 SS-15 STR-04 OMB-01 CEA-01 L-03 H-02

PA-01 PRS-01 CIAE-00 COME-00 FRB-03 INR-07 NSAEC-00

XMB-02 OPIC-03 LAB-04 SIL-01 EA-07 IO-13 /105 W

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R 091130Z SEP 76

FM AMEMBASSY BRASILIA

TO SECSTATE WASHDC 7722

INFO AMCONSUL RIO DE JANEIRO

AMCONSUL SAO PAULO

LIMITED OFFICIAL USE SECTION 1 OF 2 BRASILIA 7779

PASS TREASURY, COMMERCE, EXIM

E.O. 11652: N/A

TAGS: EIND, EFIN, BR

SUBJECT: REVELATION OF DIFFICULTIES IN BRAZIL'S STEEL

PROGRAM CAUSES ROW

REF: (A) RIO DE JANEIRO 3296, (B) STATE 221144

1. SUMMARY. WEEKEND PRESS CONTAINS TEXT OF IBRD LETTER CRITICIZING DEFICIENCIES IN THE IMPLEMENTATION OF THE CSN STEEL EXPANSION PROGRAM. SOME PRESS REACTION TO IBRD LETTER POINTS TO FOREIGN "PRESSURES", WHILE OTHER REACTION IS MORE REASONED. PRESIDENTIAL-LEVEL BODY WAS SCHEDULED TO MEET ON SEPT. 9 TO CONSIDER THE ISSUE. END SUMMARY.

BEGIN UNCLASSIFIED

2. THE RUMORED CONCERN OVER DELAYS IN CSN'S EXPANSION PROGRAM (REF A) ERUPTED INTO A LIVELY ROW FOLLOWING THE REVELATION IN SUNDAY'S PRESS OF AN IBRD LETTER CRITICIZING

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THE IMPLEMENTATION OF THE PROGRAM. THE LETTER, DATED

AUGUST 4, AND SENT TO SEVERAL GOB MINISTERS AND GOVERNMENT STEEL OFFICIALS, ENCLOSED A COPY OF A 40 PAGE IBRD EVALUATION. IN CANDID LANGUAGE THE AUTHOR OF THE LETTER, ROBERT SKILLINGS, MADE SEVERAL IMPORTANT POINTS:

--IT IS NOT THE "USUAL BANK PRACTICE TO DISTRIBUTE INTERNAL WORKING DOCUMENTS SUCH AS THE REPORT ENCLOSED; HOWEVER, UNDER THE PRESENT CIRCUMSTANCES WE HAVE CONSIDERED IT OPPORTUNE TO MAKE AN EXCEPTION."

--"CSN IS FACING A MAJOR PROBLEM." THE COST OF EXPANDING CAPACITY BY 2 MILLION TONS PER YEAR IS NOW ESTIMATED AT 3,530 MILLION DOLLARS, OR 1,750 DOLLARS PER TON PER YEAR. THIS IS "CONSIDERABLY HIGHER" THAN COSTS OF COMPARABLE PROJECTS ELSEWHERE IN THE WORLD.

--REASONS FOR THE HIGH COSTS ARE MULTIPLE: "SLOW IMPLEMENTATION OF THE PROJECT, VERY HIGH COSTS OF CIVIL CONSTRUCTION, SUBSTANTIAL SHIFT TOWARD USE OF MORE EXPENSIVE EQUIPMENT OF BRAZILIAN ORIGIN, APPARENT INCAPACITY TO HOLD THE PROJECT WITHIN THE SCOPE ESSENTIAL FOR THE INCREASE IN PRODUCTIVE CAPACITY, AND OBSERVED WEAKNESSES IN THE ADMINISTRATION OF THE EXPANSION PROGRAM."

--"THE FINANCIAL IMPLICATION OF THESE HIGH COSTS IS AGGRAVATED BY THE GENERATION OF DRASTICALLY LESS REVENUE CAUSED NOT ONLY BY THE DELAY IN THE COMPLETION OF STAGE II BUT ALSO BY THE SMALLER INCREASE IN THE PRICE OF STEEL IN RELATION TO INFLATIONARY INCREASES IN THE COMPANY'S COSTS."

--THE BANK'S "PRINCIPAL CONCERN IS THAT, UNLESS THE CSN EXPANSION IS CAREFULLY PLANNED, THE RESULT COULD BE A MIS-ALLOCATION OF SCARCE INVESTMENT RESOURCES IN BRAZIL, AND IN THE LONG RUN, A HIGHER COST STEEL INDUSTRY, WHICH COULD AFFECT THE COMPETITIVE POSITION OF BRAZIL IN THE WORLD STEEL MARKET..."

--"WE BELIEVE THAT, UNLESS IMMEDIATE MEASURES ARE TAKEN TO REDUCE THE COST OF THE EXPANSION PROGRAM, AND TO IM-LIMITED OFFICIAL USE

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PLEMENT IT EFFICIENTLY, THE CURRENT, ALREADY ACUTE SITUATION COULD DETERIORATE FURTHER, AND THE UNDESIRABLE CONSEQUENCES CITED ABOVE COULD COME TO MATERIALIZE."

--"WE ARE CONVINCED THAT YOU" (PLANNING MINISTER VELLOSO IN THE CASE OF THE PUBLISHED LETTER) "SHARE OUR CONCERNS," AND "WE HAVE NO DOUBT" THAT THE GOB AND CSN "WILL TAKE, AS THEY HAVE IN THE PAST, OPPORTUNE MEASURES TO ASSURE

THE CONTINUED GROWTH OF THE STEEL SECTOR IN AN ECONOMIC WAY."

THE LETTER ASKS FOR A MEETING WITH THE IBRD STAFF AT WHICH AGREEMENT COULD BE REACHED ON MEASUREES TO RESOLVE THIS SITUATION. (ONE SEPT. 8 PRESS REPORT CLAIMS AN IBRD TEAM, LED BY SKILLINGS, WILL COME TO BRAZIL ON SEPT. 14) END  
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3. COMMENT. IT IS UNCLEAR HOW THE LETTER WAS LEAKED OR RELEASED TO THE PRESS. THE EXPECTED (SINCE ACCOMPLISHED) RESHUFFLE OF CSN LEADERSHIP (REF A) MIGHT HAVE ENCOURAGED SOMEONE TO RELEASE IT. THE RESHUFFLE ISSUE DREW POLITICAL INTEREST LAST WEEK: AN OPPOSITION SENATOR (ITAMOR FRANCE, MDB-MG) ASKED FOR AN OFFICIAL EXPLANATION OF REASONS FOR THE RELEASE OF CSN DIRECTORS (HIGH MANAGEMENT OFFICIALS); A FREQUENT GOVERNMENT SPOKESMAN IN CONGRESS (SENATOR VIRGILIO TAVORA, ARENA-CE) REPLIED THAT THE IBRD LETTER WAS NOT THE REASON, RATHER DIVERGENCES BETWEEN CSN LEADERSHIP AND THE HOLDING COMPANY (SIDERBRAS) WERE RESPONSIBLE. THE MANAGEMENT SHAKE-UP MAY ALSO HAVE BEEN ASSOCIATED IN PART WITH TECHNICAL DIFFICULTIES AT A RECENTLY-INAUGURATED FURNACE AT CSN. THE JAPANESE, WHO PROVIDED THE EQUIPMENT, ARE REPORTEDLY BLAMING THE BRAZILIAN SIDE FOR TRYING TO RUSH THE COMPLETION OF THE WORK IN TIME FOR INAUGURATION BY PRESIDENT GEISEL ON BRAZIL'S LABOR DAY. THE JAPANESE HAVE ALLEGEDLY REFUSED TO MAKE THE NECESSARY REPAIRS UNLESS THEY ARE PAID AN ADDITIONAL SUM.

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R 091130Z SEP 76  
FM AMEMBASSY BRASILIA  
TO SECSTATE WASHDC 7723  
INFO AMCONSUL RIO DE JANEIRO  
AMCONSUL SAO PAULO

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PASS TREASURY, COMMERCE, EXIM

4. THE RELEASE OF THE LETTER HAS GIVEN RISE IN SOME PARTS OF THE PRESS TO INFERENCES OF THREATS TO NATIONAL INDEPENDENCE, AND OF FOREIGN "PRESSURES" AGAINST THE GOB'S EFFORTS TO FORCE AN INCREASE IN THE USE OF BRAZILIAN-MADE EQUIPMENT IN THE STEEL EXPANSION PROGRAM (UP TO 50 PERCENT IN PHASE III). (THERE ARE SUBSTANTIAL PRIVATE SECTOR PRESSURES ON THE GOB TO REQUIRE GREATER USAGE OF BRAZILIAN-MADE EQUIPMENT IN LARGE GOVERNMENT INVESTMENTS.) ONE BRASILIA PAPER CALLED THE LETTER "BLACKMAIL". WE WOULD NOT DISCOUNT THAT CERTAIN ELEMENTS WOULD SEEK TO TIE "FOREIGN PRESSURES" TO U.S. UNHAPPINESS WITH THE POOR PERFORMANCE OF U.S. FIRMS IN SECURING EQUIPMENT CONTRACTS FOR THE STAGE III EXPANSION PROGRAM.

5. THE RESPONSIBLE PRESS HAS TREATED THE ISSUE WITH GREATER SERIOUSNESS, AND CALLED FOR AN EXAMINATION OF THE PROBLEMS. THE JORNAL DO BRASIL, FOR INSTANCE, POINTED TO HIGH COSTS OF LOAL EQUIPMENT, AND CITED THE INEFFICIENT BUREAUCRACY AS TRYING TO CONFUSE PUBLIC OPINION BY APPEALING TO NATIONALISM TO COVER LIMITED OFFICIAL USE

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UP ITS OWN INEFFICIENCY.

6. MINISTERIAL REACTIONS HAVE BEEN DEFENSIVE, PARTICULARLY WITH RESPECT TO THE GOALS FOR USE OF NATIONAL EQUIPMENT. CONGRESS IS REPORTEDLY CONSIDERING CALLING THE MINISTERS OF PLANNING, AND INDUSTRY AND COMMERCE TO TESTIFY.

7. ACTION REQUESTED. EMBASSY WOULD APPRECIATE RECEIVING COPY OF IBRD REPORT IF IT CAN BE OBTAINED.

8. COMMENTS DIRECTED SPECIFICALLY AT QUESTION RAISED STATE 221144 WILL BE SENT BY SEPTEL.  
CRIMMINS

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## Message Attributes

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**Capture Date:** 01 JAN 1994  
**Channel Indicators:** n/a  
**Current Classification:** UNCLASSIFIED  
**Concepts:** INDUSTRY, STEEL, PRESS COMMENTS, PROGRAMS (PROJECTS)  
**Control Number:** n/a  
**Copy:** SINGLE  
**Draft Date:** 09 SEP 1976  
**Decaption Date:** 01 JAN 1960  
**Decaption Note:**  
**Disposition Action:** RELEASED  
**Disposition Approved on Date:**  
**Disposition Authority:** greeneet  
**Disposition Case Number:** n/a  
**Disposition Comment:** 25 YEAR REVIEW  
**Disposition Date:** 28 MAY 2004  
**Disposition Event:**  
**Disposition History:** n/a  
**Disposition Reason:**  
**Disposition Remarks:**  
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**Drafter:** n/a  
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**Previous Handling Restrictions:** n/a  
**Reference:** 76 RIO DE JANEIRO 3296, 76 STATE 221144  
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**TAGS:** EIND, EFIN, BR, IBRD  
**To:** STATE  
**Type:** TE  
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